



Via email to regcomments@ncua.gov

March 9, 2010

The Honorable Debbie Matz
Chairman, National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

The Honorable Gigi Hyland
Board Member, National Credit Union Administration

The Honorable Michael E. Fryzel
Board Member, National Credit Union Administration

Re: Comments on the Proposed Revision of Part 704

To Chairman Matz, Board Member Hyland, and Board Member Fryzel:

California Coast Credit Union appreciates the opportunity to submit its comments on NCUA's Proposed Rule for Corporate Credit Unions. We commend the NCUA Board and staff for its efforts to temporarily stabilize the corporate system and for working to strengthen the corporate system so that it may provide important services to natural-person credit unions in the future.

California Coast Credit Union, with assets that exceed \$1.8 billion, is the oldest credit union based in San Diego County and currently serves over 120,000 members in San Diego and Riverside County. While currently a member of two corporate credit unions, our utilization of our primary corporate, Western Corporate Federal Credit Union (WesCorp), is limited in scope due to our concern regarding their future viability of operations. In that regard, we urge the NCUA Board to quickly address the significant capital impairment that currently exists in the corporate system prior to finalizing any regulation that effectively defines their future operations.

In its entirety, the proposed regulation if enacted will significantly restrict a corporate credit union's ability to operate as a value-added going concern. This in turn will result in many natural person credit union's pursuit of both payment system and investment alternatives from multiple providers at a cost that is likely to be significantly greater. These additional costs will in all likelihood be passed on to natural person credit union members in the form of higher fees or rates. In addition, the proposed rule significantly limits a corporate credit union's ability to generate sufficient earnings to retain and build a buffer to member contributed capital. For these

reasons, we urge the NCUA to withdraw the proposal as drafted so that a more cohesive and feasible set of rules can be proposed.

California Coast Credit Union is restricting its comments to only those proposed rules that if not modified significantly, will likely have harmful effects on natural person credit unions or would effectively eliminate a corporate's ability to operate on an on-going basis.

1. Retained Earnings Growth Model

The investment portfolio diversification and spread assumptions contained in the proposed rule is ineffective at both limiting risk and creating sustainable net-interest margins. The proposed rule simply does not allow a corporate credit union to build sufficient retained earnings to meet the proposed capital ratios. The NCUA's model appears to suggest that a corporate would invest 30 percent of its entire investment holdings in student loan securitizations and 75 percent of its interest income, and therefore the vast majority of its net income would be reliant on this sector. Further, two-thirds of that 30 percent would be invested in FFELP student loans and one-third of the 30 percent would be invested in private student loans. The NCUA should be aware that private student loans are mostly unsecured loans, illiquid and require significant due diligence and credit analysis as default rates can vary significantly. In addition, net margins on FFELP student loans can vary significantly each quarter and their rates can lag market interest rates. The proposed model containing student loans, by itself, presents too much exposure from both a risk and return perspective.

A second area of concern regarding the NCUA's model is the lack of any cost of capital in its assumptions. Surely corporate credit unions will require contributed capital as a necessary component of total capital, and it would then seem necessary for the corporate to pay a return on that capital that is consistent with the risk of the contributed capital. This is amazingly absent from the NCUA model and therefore calls into question the NCUA's thoroughness in preparing this proposed rule.

We recommend that the NCUA carefully undertake a process of developing concentration limits on liquid investments sectors based on historical defaults and proven methods of stressing embedded credit protections. An independent, third-party validation of this or any other alternative model is also necessary to provide reassurance and credibility.

2. Average-Life NEV Testing

Similar to the results corporate credit unions would experience with the proposed retained earnings growth model (above), we believe the proposed average-life NEV testing would result in much the same. That is, the proposed rule requiring a credit spread widening test of 300 basis points, coupled with a NEV ratio decline limited to 15 percent, a test on slowing down prepayment speeds by 50 percent and a portfolio/asset weighted average life limit of two years does not allow a corporate to generate sufficient and sustainable net-interest margins. While we

do not take exception to a realistic credit spread widening test nor a test that slows prepayment speeds, limiting the portfolio/asset to a two year average life and an NEV ratio decline of 15 percent, would seem to limit a corporate credit union's activities to providing only overnight or very short-term investment alternatives to member credit unions. It is also unlikely that corporates could provide competitive market-based returns on member invested funds.

We recommend that the NCUA establish NEV limits consistent with that established for natural person credit unions and extend the average-life limit to a more appropriate limit consistent with other regulated financial institutions.

3. Premium for Early Withdrawals on Corporate Certificates

The proposed rule limits a corporate credit union's ability to pay a market-based early redemption price to no more than par, thus eliminating a potential source of liquidity to all certificate holders. All other things being equal, such as yield, this provision alone is sufficient reason to NOT invest surplus funds in corporate credit union certificates. Alternatively, the required spread above more liquid investments should this provision be enacted would appear to wipe out any net-interest margin earned. Said another way, corporate certificates could not be issued at a rate that is flat to Libor if this provision was included. Again here, the NCUA's model assumptions would appear to NOT be valid.

We recommend that this provision in the proposed rule be eliminated and that corporates be permitted to pay market-based prices on certificate redemptions. Certainly if the corporate has appropriately run a "matched" investment book as this proposed regulation steers them, then redeeming a certificate at a premium, if appropriate, would not cause any harm to the corporate.

In closing, California Coast Credit Union thanks the NCUA Board for the opportunity to provide our comments and recommendations regarding this proposed rule. To reiterate our comments on this proposed rule, several provisions if enacted as proposed, will have a harmful impact on natural person credit unions and effectively eliminate a corporate's ability to operate on an on-going basis. In addition, we repeat our recommendation that the NCUA quickly address the impaired corporate credit union capital and legacy assets prior to finalizing any corporate credit union regulation. Finally, we also ask that member credit unions be given a real voice in providing the direction for determining what the corporate network shall be in the future.

Sincerely,

A handwritten signature in cursive script, reading "Marla K. Shepard".

Marla Shepard
President/CEO
California Coast Credit Union